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Proposed Tariff(s) Considered TARIFF 17.A IN 1996, 1997, 1998, 1999 AND 2000

Statement of Royalties to be collected by SOCAN for the public performance or communication to the public by telecommunication, in Canada, of musical or dramatico-musical works

Reasons for decision

I. INTRODUCTION

These reasons deal with Tariff 17.A of the Society of Composers, Authors and Music Publishers of Canada (SOCAN) for the years 1996 to 2000. The tariff sets royalties for the communication to the public by telecommunication of musical or dramatico-musical works by specialty and pay television services. The filing of the proposed tariffs, their publication in the *Canada Gazette* and the notice dealing with the right to file objections to the proposed tariffs were made in accordance with section 67.1 of the *Copyright Act* (the "*Act*").

Initially, several programming and distribution undertakings raised objections to the proposed tariffs. The parties having reached an agreement among themselves and with SOCAN on a number of issues, only the pay television services, Shaw Communications, Shaw Cablesystems, the Canadian Cable Television Association, Bell ExpressVu and Star Choice Communications (direct broadcasting satellite or DBS operators), as well as the Arts & Entertainment Network and CNN, took an active part in the proceeding. The pre-hearing conference, hearing and argument took place over seven days, ending on September 27, 2000.

II. HISTORICAL OVERVIEW

On April 19, 1996, the Board issued its first decision regarding specialty and pay television services for the years 1990 to 1995.[1] The key elements of the decision provided for the payment of royalties by the transmitter rather than the services; the setting of a royalty per subscriber for the whole portfolio of Canadian specialty services; tiering of the royalty for systems serving 6,000 subscribers or less (only those with more pay the full amount); and the setting of a royalty equal to 2.1 per cent of subscription revenues for non -portfolio services (pay television and American specialty).[2] Two applications for judicial review of the decision were denied by the Federal Court of Appeal on January 15 and December 11, 1997.

Subsequently, the examination of proposed tariffs for the years 1996 and beyond was put on hold so as to allow lengthy and difficult negotiations between SOCAN, the transmitters and the services to take their course. The parties reached an agreement, inter alia, on the collection of royalties, their apportionment among transmitters and services and among the latter.[3] These negotiations and other dealings aimed at reaching an agreement on a tariff for the years 1996 and beyond, delayed the collection of royalties beyond the prescribed time-frames.

In the interim, the situation as it stood at the time of decision 17.A, 1996 has changed dramatically. First, the number of signals covered by Tariff 17.A and the revenues they generate have more than doubled, while their audience share has increased by more than half.[4] Second, the Board reduced from 2.1 per cent to 1.8 per cent the share of revenues that conventional commercial television stations pay to SOCAN.[5] Third, the number of subscribers to DBS services in Canada increased from a few thousand to over one million.

SOCAN, the transmitters and the services have agreed on several issues covered in the tariff. They propose to maintain the current formula for Canadian specialty services. They agree to more than double the royalties over five years. They further agree to maintain at its 1995 level the amount of royalties payable in 1996 for non-portfolio services. Finally, they agree to ask the Board to address only the issue of the amount of royalties payable for non-portfolio services for the years 1997 to 2000, basically to decide whether or not the reduction which conventional stations enjoyed pursuant to decision 2.A, 1998 should be reflected in Tariff 17.A.

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[1] *Statement of Royalties to be Collected by SOCAN for the Performance or Communication by Telecommunication, in Canada, of Musical or Dramatico-Musical Works under Tariff 17 for the Years 1990 to 1995*, www.cb-cda.gc.ca/decisions/m19041996-b.pdf; 70 C.P.R. (3rd) 501 [decision 17.A, 1996].

[2] Pursuant to the *Act*, the decision also establishes a preferential rate for small systems.

[3] Although the tariff specifies that the transmitter is required to pay royalties, paragraph 2.4(1)(*c*) [formerly subsection 3(1.4)] of the *Act* provides that the services are jointly and severally liable for the debt.

[4] From 1994 to 1999, the number of services increased from 40 to 85 (Exhibit SOCAN-5, Part A), revenues from $353 millions to $880 millions (Exhibit SOCAN-7) and viewing share from 19.94 to 33.17 per cent (Exhibit SOCAN-9).

[5] *Statement of Royalties to be Collected by SOCAN for the Performance or Communication by Telecommunication, in Canada, of Musical or Dramatico-Musical Works under Tariff 2.A (Commercial Television Stations) for the years 1994 to 1997*, decision of January 30, 1998, www.cb-cda.gc.ca/decisions/m30011998-b.pdf; 83 C.P.R. (3d) 141 [decision 2.A, 1998].

III. EVIDENCE AND POSITIONS OF THE PARTIES

The record includes testimony by experts, representatives of the DBS industry, and a SOCAN manager. The experts (Messrs. Ellis, Liebowitz, Fraser, Hollander and Goldstein) debated the appropriateness of using as a starting point, for the calculation of royalties, either decision 17.A, 1996 or decision 2.A, 1998; the applicability of the reasons for decision 2.A, 1998 to specialty services; and the position of American specialty services in the Canadian television universe. Representatives of the DBS industry (Messrs. Gibson and Armstrong) described the differences between DBS undertakings and conventional cable companies, i.e., fully digital transmission; ability to reach under -served subscribers; ability to tailor a package of signals to a subscriber's taste. DBS has greatly increased this number of subscribers to specialty services and especially to pay television services. The SOCAN manager, Mr. Victor Perkins, addressed the status of royalty collection as well as other issues of an administrative nature.

SOCAN argues that the 2.1 per cent rate set by decision 17.A, 1996 should be used as a starting point. As the Board noted in its second decision on retransmission in 1993, a regulatory price, once set, can acquire a life of its own.[6] The parties concur that no change occurred in the past five years in the use of music by non-portfolio services; nor has there been any change in the other factors relating to the setting of a price. It follows that the rate should remain unchanged. Subsidiarily, even if there were a perceived need to review the reasons behind decision 2.A, 1998, they are not relevant to non-portfolio services. SOCAN also argued that the use of American specialty signals in the Canadian market involves a number of features such that they are even less deserving of a reduction in royalties than any other service.

The objectors see the 2.A tariff as a starting point. They argue that the reasons which led the Board in 1996 to establish a link between the two sectors of the commercial television industry are even more compelling than before. The issue before the Board is not why the tariff paid by conventional television stations has decreased from 2.1 per cent to 1.8 per cent. Unless the reasons that led to this decrease challenge the nature of the links that the Board had identified between the two sectors in decision 17.A, 1996, the Board needs only to acknowledge the change. Even reflecting on the reasons that brought the Board to the determination it made in decision 2.A, 1998, it is plain that they apply also in the pay and specialty television marketplace. The rate should therefore drop to 1.8 per cent regardless of the approach taken. Finally, the conclusions reached by the objectors with respect to the status of American specialty signals in the Canadian marketplace are diametrically opposed to those of SOCAN.

DBS operators, for their part, further argue that the rate should discount what they characterize as a DBS dividend or digital dividend.

IV. TARIFF FOR SERVICES THAT FORM PART OF THE PORTFOLIO

The certified tariff reflects the terms of the agreement reached by the parties, including the

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[6] *Statement of Royalties to be Paid for the Retransmission of Distant Radio and Television Signals in 1992, 1993 and 1994*, decision of January 14, 1993, (1990-1994) *Copyright Board Reports* 135, p. 159, www.cb-cda.gc.ca/decisions/r14011993-b.pdf; 47 C.P.R. (3rd) 327.

extension of the Francophone market discount to DBS operators.[7] As far as the portfolio is concerned, the results obtained fall clearly within a reasonable range. Payment of the royalties provided under the agreement will not create a competitive imbalance in the television market; on the other hand, any change to the agreement may lead to disruptions. The parties have developed complex collection and allocation mechanisms and fulfilled their obligations, pursuant to the agreement. Any change to the situation would entail considerable costs and inconvenience.

This having been said, and given the reasons underpinning this decision, the participants may well want to consider the possibility of adopting, over the short or medium term, a tariff for portfolio services that is based on the tariff applicable to non-portfolio services.

V. NON-PORTFOLIO SERVICES

The Board does not believe that it is necessary, at this point, to engage debate over the notion of proxy and whether or not it should be used once a price has been established.[8] As the Board noted in decision 17.A, 1996, conventional television broadcasters and specialty services "…operate in similar industries, competing for the same inputs, and offering viewers a similar product: programming. ...The tariff for one should not create a competitive imbalance between the two players." [9] The Board believes that the best way to achieve competitive balance is to ensure that, all things being equal, a single price is applied equally to the entire commercial television industry – conventional or other.

The market for conventional television and the market targeted in this current tariff are one and the same. Operators within the same industry should face the same input costs. It is therefore the intention of the Board, in the current decision, to move towards the convergence of the tariffs applicable to both of these sectors. Seen from another angle, and unless there is evidence to the contrary, the best way to promote consistency, which the Board has striven to attain since 1991[10] and even earlier, would be to merge the tariffs. This decision is a step in that direction.

There can be no doubt that differences exist between conventional television and specialty and pay television services. Pay television, for example, is first and foremost concerned with subscriber churn [11] as opposed to viewership; the record of these proceedings shows clearly that many subscribers are prepared to pay for services that they very seldom use. But still,

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[7] In its most recent decision on retransmission, the Board refused to grant such a discount: *Statement of Royalties to be Collected for the Retransmission of Distant Radio and Television Signals in 1998, 1999 and 2000*, decision of February 25, 2000, www.cb-cda.gc.ca/decisions/r25022000-b.pdf; 5 C.P.R. (4th) 440.

[8] Those who think that the Board used a proxy price in 1996 are not necessarily right. Throughout the entire decision, the matter is discussed in terms of comparisons, but nothing more. Moreover, neither the term "proxy price" nor its French equivalent "*prix de substitut*" are ever encountered, although both are native to other decisions of the Board.

[9] *Supra*, Note 1, p. 18 (Internet), pp. 517h-518a (C.P.R.).

[10] *Statement of Royalties to be Collected by SOCAN for the Public Performance in Canada of Musical or Dramatico-Musical Works in 1991*, July 31, 1991 decision, *Copyright Board Reports* 281, 291-293, www.cb-cda.gc.ca/decisions/m31071991-b.pdf; 291-293; 37 C.P.R. (3rd) 385, 392c-394b.

[11] Conventional television sells ads based on the number of viewers and their demographics. Pay television convinces viewers to pay for access to programming, whether or not they watch it.

convergence factors (the nature and source of inputs, for example) are clearly predominant. We are even witnessing this in other respects. Thus in decision 17. A , 1996, the Board adjusted the amount of royalties to reflect the fact that specialty services spent a smaller portion of their revenues on programming compared with conventional television.[12] As confirmed by Exhibit Board-2 , the ratio is now virtually identical.

An examination of the factors that led the Board to rule as it did in decision 2.A, 1998 strengthens the conclusion that we are in fact dealing with one and the same industry. Whether or not one agrees that the value of the SOCAN licence for conventional television broadcasters has decreased, it is plain to see that this value is the same for both sectors of the industry; moreover, the parties concur on this point. Likewise, whether or not one agrees that the political and economic environment in which conventional television broadcasters operate has evolved, again it is evident that all programming undertakings operate in the same environment, including those, like the services, whose very presence explains in large part the changes that may have occurred in this environment. Setting a different price for any specific sector would necessarily lead to a market imbalance.

This is not to say, however, that the rate applicable to all television broadcasters will always be the same. At least two factors might trigger an upward or downward adjustment if some sector of the industry, or even a single undertaking, were to sufficiently stand out in this respect. The first factor is the use of music, more specifically the amount of protected music used.[13] The second is the portion of operating expenses attributable to programming expenditures [14] or the portion of programming expenditures accounted for by the royalties paid to SOCAN.[15] The parties agree that there are no significant differences in these regards between the services and conventional television at the moment.

It does not follow from this decision that Tariff 17.A now depends on Tariff 2.A. In this instance, the Board must act to prevent a market imbalance. Other proceedings may provide the opportunity to address the issue of merging these tariffs or using other means to ensure that all television broadcasters, regardless of differences in the rate formula, will pay more or less the same price for music. Common hearings for the entire industry may be desirable.

As previously mentioned, the parties have agreed that the 1996 tariff for non -portfolio services would be the same as the 1995 tariff, or 2.1 per cent. The reasons which the Board puts forward for ruling as it does for the years 1997 to 2000 (i.e., 1.8 per cent) would have also led it to certify the tariff for 1996 at the negotiated rate of 2.1 per cent.

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[12] *Supra*, Note 1, pp. 20-21 (Internet), pp. 519f-520a (C.P.R.).

[13] This is the key factor which led the Board to rule as it did with respect to the CBC [among others, *supra*, Note 10, pp. 311-312 (C.B.R. and Internet), 408f-409f (C.P.R.)] and in the matter of SODRAC-MusiquePlus inc., www.cb-cda.gc.ca/decisions/a16112000-b.pdf

[14] A similar factor had led to a reduction of the tariff applicable to portfolio services in decision 17.A, 1996: *supra*, Note 10.

[15] It is on the basis of this factor that the Board established the proportion of retransmission royalties paid to SOCAN. See, for example, *supra*, Note 6, pp. 189-190 (C.B.R. and Internet), 373d-374f (C.P.R.).

Tariff 2.A was certified for 1997, but has yet to be certified for subsequent years. A decision of the Federal Court of Appeal would have allowed certification of a tariff for non-portfolio services which would be based on the decision to be made regarding Tariff 2.A.[16] It is not the intention of the Board to proceed in this way. The number of participants, the complexity of the mechanisms for sharing the burden of royalties and the requirement for SOCAN to proceed with regular distributions bearing the stamp of finality, are so many factors which warrant the conclusion that it is preferable to issue a final ruling rather than allow readjustments to payments several years after the fact.[17] Although the decision compels SOCAN to make some reimbursements, it has the merit of resolving the matter.

VI. THE DIGITAL DIVIDEND

DBS operators rightly claim that they provide viewers some benefits such as better picture, better sound and more choice, that have little to do with the intellectual property they deliver. They add that some of the growth in the number of subscribers to non-broadcast services, and especially pay television, is due in large part to their efforts to reach new markets and offer better delivery, not to any increase in the value of the underlying copyrights. They question whether rights holders should reap any benefits from such efforts.

This is a non-issue. Royalties payable pursuant to Tariff 17.A are based only on what transmitters, including DBS undertakings, pay for programming. No account is taken of their revenues. Furthermore, any benefits that copyright owners of music may reap as a result of DBS undertakings expanding market demand for non-broadcast signals are no more, no less, than the benefits so reaped by other suppliers of creative inputs, including the services themselves.

Claude Majeau
Secretary General

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[16] *Canadian Broadcasting Corp.* v. *Canada (Copyright Board)*, [1993] F.C.J. No. 227; (1993) 47 C.P.R. (3rd) 426 (C.A.). As the Board does not use this formula, there is no need to go into the reasons which would lead the Board to dismiss the arguments that were contrary to the objectors'.

[17] Similar reasons led the Board, in its decision 2.A, 1998, to not reduce the tariff for the years 1994, 1995 and 1996: *supra*, Note 5, pp. 17-18 (Internet), 155-157 (C.P.R.).